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Given this sweet arrangement, it is no wonder that the pharmaceutical industry is one of the most profitable business sectors in modern history. In 2013, five major pharmaceutical companies made a profit margin of 20 percent or more, and several regularly have profit margins of greater than 30 percent. Every business aims to make a profit, but let us consider those numbers in context. Pharmaceutical corporations make a return on their assets that is more than double the average of all the Fortune 500

PHARMACEUTICAL CORPORATIONS REAP HISTORY-MAKING PROFITS

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companies. In the past decade, the top ten pharmaceutical companies made more in profits than the rest of the Fortune 500 companies combined. Year after year, rankings of the most profitable industries reliably put pharmaceutical corporations at the very top or close to the top, higher than legendary money makers such as banks and oil companies.

I discuss later (chapters 16, 17, and 22) how longtime moral and legal traditions suggest that medicines research, manufacturing, and distribution should not be dependent on a for-profit scheme. But even many who believe a profit motive has a place in our medicines system are convinced that the level of profits in the pharmaceutical industry rises far above what is reasonable and appropriate, especially given the human cost incurred.

Pfizer, the world’s largest pharmaceutical company, provides a good example of the cash-flush nature of the industry. In 2013, Pfizer reported a 42 percent profit margin, a return that the BBC characterized as “eye-watering,” part of a two-year stretch during which the company generated over $9 billion annually in net profits. Do you remember (chapter 3) that Ahmed and millions of children die each year because of a lack of affordable vaccines? One of the top Pfizer product lines is vaccines, and the corporation earns more than $17 million each day in sales from its pneumonia vaccine alone.

Pfizer is a prominent member of PhRMA, which spends significant industry money putting forth the argument that its member companies take enormous business risks. “Biopharmaceutical R&D is an extremely complex process and failure is more common than success,” according to PhRMA. But that argument is undermined by the year-after-year industry record of world-leading profits. As Alan Sager, Boston University health economist, puts it, “If you went to Las Vegas with $1,000 and routinely came back with $1400, could your family accuse you of gambling?”

What do pharmaceutical corporations do with their billions in windfall profits? Although industry public relations would have us believe the companies put that money into research and development, many highly profitable corporations have reduced their research investments in recent years. Marianna Mazzucato, an economist, says this is a predictable result of a system that allows private industry to benefit from government investments in research—called free-riding. So, instead of ramping up their research and development, pharmaceutical corporations spend billions in financial maneuvers such as buying back shares of their own stock. Pfizer again provides a good example of this practice. Between 2003 and
2012, the company spent $59 billion of its profits in stock buybacks. In 2014 alone, Pfizer spent almost $12 billion to buy back its own shares and to pay dividends to its shareholders—financial transactions that added up to almost 50 percent more than the company spent on research and development.

Why do Pfizer and other drug companies buy back their own stock? To the public, corporate CEOs provide one answer. When he announced a $10 billion stock buyback in 2011, Ian Read, the Pfizer CEO, said the plan was “a testament to our continued commitment to enhancing shareholder value and to our continued confidence in the business.” In other words, pharmaceutical stock is so valuable, we want more of it for ourselves.

But in truth, stock buybacks are conducted because they benefit the two most powerful forces in pharmaceutical industry: shareholders and top executives. First, stock buybacks lift the company stock price (note the reference to “enhancing shareholder value” by Read), which makes shareholders happy. Second, buybacks that lift stock values make pharmaceutical company CEOs even happier because their salaries are typically tied to the price of the company stock.

CEOs and other top executives are the big winners in the stock-buyback scheme, which is a core reason why the pay of high-level corporate executives has more than doubled since the early 1990s. Over the course of the 2003–2012 decade, the largest eleven pharmaceutical companies paid their CEOs a combined salary of $1.57 billion. In 2015, the average compensation for CEOs of the large pharma corporations was over $18 million, 71 percent more than the average of other large corporations.

Big profits and big salaries may seem relatively harmless until we consider that millions die because they cannot afford the products these corporations produce. A 2016 analysis published in the BMJ (formerly the British Medical Journal) tied high drug prices, along with reduced research investments, to the current pharma business model of buying products developed elsewhere and then devoting revenue to rewarding stockholders and top executives. In a 2014 article for the Harvard Business Review, the health economist William Lazonick reviewed the status of profits, stock buybacks, and executive pay. He concluded that the data make a mockery of the pharmaceutical industry claim that it needs high profits to fund research and development. “The reality is,” Lazonick wrote, “Americans pay high drug prices so that major pharmaceutical companies can boost their stock price and pad executive pay.”